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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 28

IN THE MATTER

of

FLORIDA EAST COAST RAILWAY COMPANY,

Debtor,

J. BRYSON AIRD and BANK OF THE MANHATTAN COMPANY, Successor Mortgage Trustees,

Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD COMPANY,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF ON BEHALF OF J. BRYSON AIRD AND BANK OF THE MANHATTAN COMPANY, SUCCESSOR MORTGAGE TRUSTEES, PETITIONERS

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 36

IN THE MATTER

of

FLORIDA EAST COAST RAILWAY COMPANY,
Debtor,

J. BRYSON AIRD and BANK OF THE MANHATTAN COMPANY,
Successor Mortgage Trustees,
Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF ON BEHALF OF J. BRYSON AIRD AND BANK OF THE MANHATTAN COMPANY, SUCCESSOR MORTGAGE TRUSTEES, PETITIONERS

Opinions Below

The opinion of the District Court (R. Vol. I, p. 127) is reported in 103 F. Supp. 825.

The opinion of the Court of Appeals (R. Vol. II, p. 717) is reported in 201 F. 2d 325.

An earlier opinion of the District Court on the immediately preceding plan of reorganization of the debtor is reported in 81 F. Supp. 926.

The opinion of the Court of Appeals on that plan is reported in 179 F. 2d 538.

Jurisdiction

The judgment of the Court of Appeals was entered January 19, 1953. The petition for certiorari was filed April 9, 1953, and granted May 4, 1953. The jurisdiction of this Court rests upon Title 28, U. S. C., § 1254.

Question Presented

This Court granted certiorari on May 4, 1953, in the following terms: "Granted limited to Question I presented by the petition for writ of certiorari in No. 670", No. 670 being the petition for certiorari filed on behalf of the St. Joe Paper Company and others. We therefore turn to that petition to ascertain the limitations on the grant of certiorari; and in particular to the specification of error under Question I, which reads as follows:

> "The Court of Appeals erred (I) in construing Section 77 of the Bankruptcy Act as amended in 1935 to grant the Interstate Commerce Commission power to propose and certify a plan of reorganization involving a consolidation or merger of the Florida East Coast Railway Company with the Atlantic Coast Line, to which the Florida East Coast Railway had not agreed, and in approving such a plan over the objection and protest of 99% of the equitable owners of the Florida East Coast Railway." (St. Joe Petition, p. 3)

We appreciate that this Court has narrowed the issue on this appeal to a single question concerning the powers of the Interstate Commerce Commission. But we do not

construe the grant of certiorari to be on a wholly abstract question, and respectfully submit that the question should be considered in the light of certain facts in the record relating to this particular reorganization, the most important of which are:

(1) that the bondholders referred to in St. Joe's petition for certiorari as "the equitable owners of the Florida East Coast Railway" are the bondholders whose bonds were issued under a First and Refunding Mortgage dated September 1, 1924, under which the petitioners whom we represent on this appeal are the Mortgage Trustees;

(2) that the mortgage security consists of substantially all the assets of the Florida East Coast Railway;

(3) that by Florida law the Mortgage Trustees are entitled to look to the mortgaged assets in satisfaction of the mortgage debt, which exceeds $80,000,000; and

(4) that the consideration passing from the Atlantic Coast Line has a fair market value which is less than the mortgage debt.

The question presented from the point of view of the petitioners, Mortgage Trustees, is, therefore, as follows:

Does Section 77 authorize the Interstate Commerce Commission in a reorganization proceeding to transfer to another railroad against the mortgagee's consent substantially all of the debtor's assets pledged as security for the mortgage debt at a price fixed by the Commission that is less than the mortgage debt?

Statutes Involved

The pertinent provisions of Section 77 of the Bankruptcy Act, together with pertinent provisions of the mortgage involved, appear in the Appendix, pp. 24-31, *infra*.

Specification of Errors

The Court of Appeals erred in construing Section 77 to authorize the Interstate Commerce Commission in a reorganization proceeding to transfer to another railroad against the mortgagee's consent substantially all of the debtor's assets pledged as security for the mortgage debt at a price fixed by the Commission that is less than the mortgage debt.

Statement

In the brief submitted on behalf of the St. Joe Paper Company, petitioner, there is to be found a Statement with which we are in full accord, and adopt. However, since our argument on behalf of the petitioners, Mortgage Trustees, is not intended to duplicate the argument of the St. Joe Paper Company, additional facts necessary to a full grasp of our argument follow:

The debtor, Florida East Coast Railway Company, is a Florida corporation whose tracks run south of Jacksonville. Consequently all of its fixed assets and substantially all of its rolling stock and intangible assets are located in Florida. It has no railroad subsidiaries or affiliates. It operated under an equity receivership in the United States District Court for the Southern District of Florida from 1931 until January 25, 1941, when the present reorganization proceeding was instituted under Section 77 of the Bankruptcy Act.

In 1909 the debtor railroad executed and delivered a First Mortgage to secure $12,000,000 principal amount of

4½% Gold Bonds. These Bonds are not in default, and all but $8,189,000 face value have been purchased by the Reorganization Trustees under authority of a court order and are held by them for the benefit of a junior issue of 5% Refunding Bonds more fully described below (103 F. Supp. 828). Additionally more than $8,189,000 cash or its equivalent has been earmarked by the Reorganization Trustees to redeem the remaining outstanding First Mortgage Bonds when a final plan of reorganization has been consummated. In point of fact, the entire First Mortgage issue would have been paid off and the Mortgage discharged four years ago had not the First Mortgage Trustees objected to the proposal on the grounds that there was no legal basis for calling the Bonds prior to their maturity except as part of the final consummation of a plan of reorganization. This senior bond issue represents no problem on this appeal.

On September 1, 1924, the debtor railroad executed a First and Refunding Mortgage to the Bankers Trust Company and one Bethune W. Jones, as Trustees, to secure an aggregate principal amount not to exceed $150,000,000 of First and Refunding 5% Bonds. A copy of this Mortgage (127 printed pages in length) can be found as Exhibit A to Document 84 in the District Court Equity Proceedings. Its pertinent provisions are set forth in the Appendix, pp. 28-31, *infra*.

Only $45,000,000 principal amount of the 5% Bonds were issued, and these are still outstanding, together with not less than $35,000,000 principal amount of accrued unpaid interest coupons. Your petitioners herein are the Successor Trustees under the First and Refunding Mortgage, having succeeded to that position in December, 1948, pursuant to the provisions of the Mortgage covering the appointment of successor trustees.

Substantially all of the assets of the Florida East Coast are subject to the lien of the First and Refunding Mortgage,

and the division of the relatively small amount of free assets among unsecured creditors will present no problem. Because adequate provision in cash or its equivalent has been made for the First Mortgage Bonds, because the equipment liens are amply secured and self-liquidating, and because of the size of the present claim of the Trustees of the First and Refunding 5% Bonds, these Trustees and their *cestuis*, the holders of the bonds, are the equitable owners of the mortgaged property (103 F. Supp. 825, 831). The petitioners herein, the Mortgage Trustees, are also the legal holders of a mortgage covering substantially all the debtor's property. This Mortgage is in conventional form containing the standard "granting", "habendum", and "grant in trust" clauses, as well as the right in event of default to enter upon and sell the mortgaged property, or to institute proceedings for judicial sale. Furthermore, the Mortgage specifically provides that upon any such sale the bonds and matured unpaid coupons may be applied against the purchase price.

The Mortgage was filed for record in the appropriate recording office of each of fifteen counties in Florida in which property of the railroad was located.

Insofar as the individual holders of the First and Refunding 5% Bonds are concerned, the record shows that at the time of the hearing in the District Court on the latest plan the holders of slightly less than $35,000,000 face value of the bonds, being 75.5% of the issue, were, by written documents filed with the Court, opposed to the reorganization plan (103 F. Supp. 847). As to the holders of the remaining $10,000,000, there is admittedly nothing to indicate how they then felt except for the few bonds then represented by a committee (since dissolved) which supported the plan. Certainly there has been no affirmative support of the plan by any bondholders who are part of this minority other than those who had bonds on deposit with the committee, and in the absence of such affirmative support the District

Court, and even the Court of Appeals in its latest opinion, accepted the fact that substantially all the bondholders are opposed to the latest plan calling for a forced merger with the Coast Line (103 F. Supp. 831-833; 201 F. 2d 326).

The petitioners, First and Refunding Mortgage Trustees, are in effect, therefore, the holders in trust of a single secured claim, the security being substantially all of the assets of the debtor.

There have been a number of plans of reorganization of the debtor certified by the Interstate Commerce Commission since 1941. The last two of these plans, one certified in March, 1948, which was subsequently disapproved, and the present plan, certified on October 25, 1951, contain a provision that the assets of the debtor, substantially all of which are pledged to the petitioners-mortgagees under the First and Refunding Mortgage, should be transferred to the Atlantic Coast Line Railroad Company in consideration of the issuance and delivery by that company for distribution to the First and Refunding Bondholders of cash and securities of the Atlantic Coast Line, the aggregate value of which has always been far less than the mortgage debt.

The question whether Section 77 authorizes a compulsory transfer to the Atlantic Coast Line of assets mortgaged to the Mortgage Trustees-petitioners came up in the courts below in respect to the earlier plan of reorganization certified in 1948. Judge Sibley, who is now retired but who at the time was a member of the Court of Appeals for the Fifth Circuit sitting as Judge Designate in the District Court for the Southern District of Florida, held that the statute did not authorize the Commission to force such a transfer (81 F. Supp. 926). On appeal Judge Sibley was in effect reversed on this point by a divided decision of two to one (179 F. 2d 538). Since then, and with respect to the present plan Judge Strum, also a member of the Court of Appeals, has clearly indi-

cated that in his opinion Section 77 does not authorize the Commission to compel this transfer of mortgaged property to a third party (although conceding it to be the law of the case that such a transfer in some circumstances is permissible) (103 F. Supp. 834, 835). In the decision here on appeal, Judges Hutcheson, Holmes and Rives answered this question in the affirmative, but Judge Russell, joined by Judge Borah, expressly stated in a dissenting opinion that a compulsory merger is not authorized by Section 77 (201 F. 2nd 325, 331-2).

In effect, therefore, four members of the Court of Appeals for the Fifth Circuit (one now retired) have answered in the negative the question here presented. Only three members of the same Court have taken the opposite view.

Summary of Argument

There are several approaches to the question presented. The first is to determine whether the language of Section 77, and in particular the so-called "consistency clause", permits an affirmative answer to the question presented, and in this connection whether the 1935 amendments to Section 77 operated to effect any important change in the application of the "consistency clause". The brief submitted on behalf of the St. Joe Paper Company which we respectfully suggest should be read first, is, in our opinion, a full and fair presentation of arguments along the lines of this first approach. The Mortgage Trustees strongly endorse the arguments so presented, and we will not burden this Court by repeating them.

Another approach to the question is to determine whether the Congress can be considered to have consciously authorized compulsory consolidations in enacting a statute (Section 77(b)(5)) despite the fact that neither the word "voluntary" nor the word "involuntary" is used in that

part of the statute cited as supporting the power to compel transfer of the debtor's mortgaged property to an outside railroad over the protests of the mortgagee.

It seems appropriate that the Mortgage Trustees should assume the burden of argument along the lines of this approach in urging a negative answer to the question presented. The fact that they are also trustees does not, for purposes of our argument, alter or affect their status as mortgagees.

As against the mortgagees of substantially all the assets of the debtor railroad acquired under a mortgage executed in 1924, eleven years before the passage of the 1935 amendments to Section 77, an affirmative answer to the question presented would seem to fall squarely within the rule enunciated in *Louisville Bank* v. *Radford*, 295 U. S. 555 (decided on May 27, 1935, some three months before the passage of the 1935 amendments to Section 77), that substantive rights in specific property acquired by a mortgagee before the passage of a bankruptcy statute could not be taken away by such statute.

The fact that the *Radford* case was decided in May, 1935, is, we shall show, far more than of merely passing interest. It bears heavily, if not conclusively, on any decision as to how far—three months after that decision—the Congress *intended* to go in expanding the powers of the Interstate Commerce Commission to expropriate vested rights.

POINT I

The forced merger provisions of the plan certified by the Commission for the Florida East Coast Railway destroy all substantive security rights given by the laws of Florida under the mortgage held by the petitioners, the Mortgage Trustees.

The petitioners-mortgagees are the Successor Trustees under a First and Refunding Mortgage which was executed on September 1, 1924. A copy of the Mortgage is part of Document 84 in the Record of the prior equity proceeding entitled "Standard Oil Company, a corporation, plaintiff, *v.* Florida East Coast Railway Company, a corporation, defendant", in Equity No. 737, United States District Court, Southern District of Florida. Pertinent provisions are set forth in the Appendix, pp. 28-31, *infra*.

Under the law of Florida, a mortgage creates a lien which may be foreclosed by suit resulting in a judicial sale of the property (Sections 697.02, 702.01 Florida Statutes, 1951; *Georgia Casualty Co.* v. *O'Donnell*, 109 Fla. 290, 147 So. 267; *Hemphill* v. *Nelson*, 95 Fla. 498, 116 So. 498; *Berlack* v. *Halle*, 22 Fla. 236, 246, 1 Am. St. Rep. 183). While mere default does not entitle the mortgagee to possession, in the action for the sale of mortgaged property a receiver may be appointed if it appears "that the land is inadequate security for the debt" or "that the mortgagor is insolvent or resides out of the State" (*Pasco* v. *Gamble*, 15 Fla. 562, 567); and, where there is a pledge in the mortgage of rents, issues, and profits, and provision for appointment of a receiver, the mortgagee "is entitled, default in the payment of interest and principal having occurred, to have the net profits derived from the mortgaged property applied to the payment of the debt and the interest thereon", and a receiver will be appointed, if necessary, to see that this is done (*Smith* v. *DuPuis*, 117 Fla. 222, 231, 157 So. 491).

If the mortgage contains an acceleration clause so providing, the mortgagee may bring suit to foreclose the mort-

gage and have the premises sold to satisfy the entire mortgage debt upon failure of the mortgagor to pay taxes on the property as agreed (*Treb Trading Co.* v. *Green*, 102 Fla. 238, 135 So. 510, 136 So. 688), or upon failure of the mortgagor to pay one of the mortgage notes at the agreed time for payment (*Hotel Management Company* v. *Krickl*, 117 Fla. 626, 158 So. 118), or upon failure of the mortgagor to pay an interest note when the same becomes due (*Graham* v. *Fitts*, 53 Fla. 1046, 43 So. 512), or upon some other default or breach of covenant, depending upon the particular terms of the individual acceleration clause. Even in the absence of such a clause, the mortgagee is entitled to file a suit to foreclose the mortgage after the time limited for payment of the principal debt has expired (*Kirk* v. *Von Petten*, 38 Fla. 335, 21 So. 286), or at any time a part of the principal or interest has become due and is not paid (*Miami Mortgage and Guaranty Company* v. *Drawdy*, 99 Fla. 1092, 127 So. 323; *Wordinger* v. *Wirt*, 112 Fla. 822, 151 So. 47). If only part of the principal or interest has become due when the foreclosure suit is brought, the land will be sold subject to the lien of the mortgage for the balance of the secured debt yet to become due, and the proceeds of the sale will be applied to payment of that part of the mortgage debt past due (*Miami Mortgage & Guaranty Company* v. *Drawdy, supra; Wordinger* v. *Wirt, supra*).

The final decree of foreclosure adjudges the equities of the parties and directs a sale of the property upon failure of the mortgagor to pay within a fixed period the amount found to be due the mortgagee (*Life and Casualty Insurance Company* v. *Tumlin*, 138 Fla. 447, 189 So. 406). Where no particular period is specified in the foreclosure decree during which the mortgagor can make satisfaction of the mortgage indebtedness, the right to redeem may be exercised at any time prior to the completion of the foreclosure sale (*Von Huss* v. *Prudential Insurance Company*, 123 Fla. 20, 165 So. 896). No statute or court decision permits the mortgagor to obtain a release or surrender of the

property from the mortgage lien without paying in full the indebtedness secured. A mortgagee may protect his interest in the property by bidding at the foreclosure sale and may apply the amount found to be due him under the final decree on his bid over and above the amount necessary to pay costs (*Tucker* v. *Crown Corporation*, 136 Fla. 517, 183 So. 740, 745).

Thus, the controlling law of Florida was and is that mortgaged property shall be devoted primarily to the satisfaction of the debt secured; and the provisions of its law are appropriate to ensure that result.

The effect of an affirmative answer to the question presented on this appeal would be that, for the rights acquired and possessed by the mortgagees under the law of Florida, only the following alternative is provided: the right to have the Interstate Commerce Commission appraise the mortgaged property by capitalizing its estimated future earnings (and which appraisal may be in a sum far less than the amount of the mortgage debt) and thereupon transfer this property, free of mortgage, to a third party railroad against the payment of the appraised value not in cash, but in securities of that railroad. In this particular case the mortgaged property is ordered to be transferred to the Atlantic Coast Line in consideration of $14,000,000 face value of Divisional First Mortgage Bonds, $13,500,000 face value of Income Divisional Mortgage Bonds, $9,000,000 par value of Atlantic Coast Line Participating Cumulative Convertible Preferred Stock, and $6,000,000 par value of Atlantic Coast Line no par Common Stock with a stated value at $100 per share, a total face value of $42,500,000 (282 I. C. C. 195, 216). The Atlantic Coast Line appears to be called upon to pay an additional $4,000,000 cash, but this payment is more illusory than real since the Coast Line will receive from the debtor's estate cash, to which the mortgagees are presently entitled, in exactly that amount ($3,000,000 for new stations; $1,000,000 for working capital) (282 I. C. C. 195, 215).

Keeping in mind that the mortgage debt is in excess of $80,000,000, we therefore find a situation where mortgaged property is being transferred to a third party, free of the mortgage lien, against the wishes of the mortgagee, and without a judicial sale, for approximately half that amount. The denial of the right of a judicial sale was an integral part of the reorganization plan certified by the Commission, for in the third supplemental report the Commission admits:

> "In any plan purporting to transfer control of the debtor to the Coast Line, a provision permitting a judicial sale of the mortgaged property * * * would defeat such a transfer, since the Coast Line obviously could not successfully compete in bidding with the debtor's first and refunding bondholders, a large majority of whom (in amount of bonds) desire to retain control." (267 I. C. C. 295, 307)

The drastic effect of the Commission's action, if approved by this Court, can hardly be better characterized than by the following excerpt from Judge Strum's opinion:

> "If persons are to be thus deprived, *in invitum*, of their lawfully held property and forced over their objection to accept in lieu thereof property of debatable value which they do not want, while the property they now lawfully own and wish to retain is awarded to a stranger who wishes to acquire it, the exercise of such a drastic and far-reaching power—approaching absolutism in Government even in the case of a public utility—should rest upon considerations more compelling than those offered by the Commission in support of its fourth plan." (103 F. Supp. 825, 835)

POINT II

In the light of the expressed disapproval by this Court, only three months before the passage of the 1935 amendments to Section 77, of legislative attacks upon substantive mortgage rights, it is wholly unreasonable to conclude that the Congress intended to authorize forced mergers when it enacted the 1935 amendments to Section 77.

We do not argue the constitutionality of the Commission's action, since this Court has refused to hear argument on that question, but we believe we are entitled to urge that the Congress could never have intended the drastic interpretation of the 1935 amendments to Section 77 that is implicit in the Commission's action. Only three months previous to the adoption of these amendments this Court had handed down its decision in *Louisville Bank* v. *Radford*, 295 U. S. 555, directed squarely against legislative attacks on substantive rights of mortgagees by means of a bankruptcy statute (Section 75 (s) of the Bankruptcy Act, as amended —also known as the first Frazier-Lemke Act); and as more fully discussed hereinafter, the same Congress, virtually contemporaneously with the passage of the 1935 amendments to Section 77, enacted a new subdivision (s) to Section 75 for the purpose of eliminating the objectionable features of the old Act condemned in the *Radford* case.

In the *Radford* case the plaintiff bank held a mortgage executed in 1924 on Radford's property. By 1933 the mortgagor had defaulted on various covenants in the mortgage, including covenants to pay installments of interest and principal. In June, 1933, the mortgagee declared the entire indebtedness immediately payable and commenced a foreclosure suit. Section 75 (s) of the Bankruptcy Act was passed in June, 1934, and in August, 1934, the mortgagor filed appropriate petitions for relief thereunder. The Paragraph Seven relief of that Section 75 (s) provided that the mortgagor could pay into court during a five-year period the appraised value of the property (of which he

had retained possession), or the court-reappraised price if the mortgagee should request a reappraisal, and thereupon the court could, by an order, restore title to the mortgagor free of the mortgage debt. In these proceedings the referee in bankruptcy ordered an appraisal of the mortgagor's property subject to the mortgagee's lien, and this was determined to be less than one-half of the amount of the mortgage. The mortgagee refused to accept payment of this amount, and the controversy eventually found its way to this Court, which upheld the mortgagee. Among other reasons for the position taken by this Court, Mr. Justice Brandeis stated (295 U. S.):

> "No instance has been found, except under the Frazier-Lemke Act, of either a statute or decision compelling the mortgagee to relinquish the property to the mortgagor free of the lien unless the debt was paid in full.
>
> "This right of the mortgagee to insist upon full payment before giving up his security has been deemed of the essence of a mortgage. His position in this respect was not changed when foreclosure by public sale superseded strict foreclosure or when the legislatures of many states created a right of redemption at the sale price. To protect his right to full payment on the mortgaged property, the mortgagee was allowed to bid at the judicial sale on foreclosure." (pp. 579, 580)
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> • • •
>
> "Statutes for the relief of mortgagors • • • were sustained by this Court when • • • they were found to preserve substantially the right of the mortgagee to obtain, through application of the security, payment of the indebtedness. They were stricken down [by this Court] • • • when it appeared that this substantive right was substantially abridged." (p. 581)
>
> • • •
>
> "By the settled practice, a sale free of liens will not be ordered by the bankruptcy court if it appears that the amount of the encumbrance exceeds the value of the property. And the sale is always made

so as to obtain for the property the highest possible price." (p. 584)

• • •

"In no case of composition is a secured claim affected except when the holder is a member of a class; and then only when the composition is desired by the requisite majority and is approved by the court. Never, so far as appears, has any composition affected a secured claim held by a single creditor." (pp. 585, 586)

• • •

"If the public interest requires, and permits, the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain: so that, through taxation, the burden of the relief afforded in the public interest may be borne by the public." (p. 602)

The *Radford* decision was handed down by this Court in May, 1935. Because economic conditions in the country called for emergency relief to farmer debtors, the Congress, after studying the decision, passed a new subdivision (s) of Section 75 (colloquially referred to as the second Frazier-Lemke Act) on August 23, 1935, just three days after the passage of the 1935 amendments to Section 77. Section 75 (s), as redrawn by the Congress in order to comply with Mr. Justice Brandeis' opinion in the *Radford* case, eliminated those sections of the earlier Act which were deemed objectionable as taking away substantive rights held by mortgagees in the specific property. In *Wright* v. *Vinton Branch*, 300 U. S. 440, the second Frazier-Lemke Act was passed upon by this Court and upheld, with an opinion also by Mr. Justice Brandeis. In that opinion Mr. Justice Brandeis restated the holding in the *Radford* case and then proceeded to demonstrate how the provisions of the second Frazier-Lemke Act were drawn in order to comply with the Court's mandate (300 U. S.):

"The [Radford] opinion enumerates five important substantive rights in specific property which had

been taken. It was not held that the deprivation of any one of these rights would have rendered the Act invalid, but that the effect of the statute in its entirety was to deprive the mortgagee of his property without due process of law. The rights enumerated were . . .

"'1. The right to retain the lien until the indebtedness thereby secured is paid.

"'2. The right to realize upon the security by a judicial public sale.

"'3. The right to determine when such sale shall be held, subject only to the discretion of the court.

"'4. The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale or by taking the property itself.

"'5. The right to control meanwhile the property during the period of default, subject only to the discretion of the court, and to have the rents and profits collected by a receiver for the satisfaction of the debt.'" (p. 457)

Of those five enumerated rights, we are, for purposes of this appeal, interested in the first four, which obviously go to the essence of the substantive rights of every mortgagee. As to the first three, Mr. Justice Brandeis stated (300 U. S.):

"It is not denied that the new Act adequately preserves three of the five above enumerated rights of a mortgagee. 'The right to retain the lien until the indebtedness thereby secured is paid' is specifically covered by the provisions in Paragraph 1, that the debtor's possession, 'under the supervision and control of the court,' shall be 'subject to all existing mortgages, liens, pledges, or encumbrances,' and that:

"'All such existing mortgages, liens, pledges, or encumbrances shall remain in full force and effect,

and the property covered by such mortgages, liens, pledges, or encumbrances shall be subject to the payment of the claims of the secured creditors, as their interests may appear.'

"'The right to realize upon the security by a judicial public sale' is covered by the provision in Paragraph 3 that at the termination of the stay:

"'. . . upon request in writing by any secured creditor or creditors, the court shall order the property upon which such secured creditors have a lien to be sold at public auction.'" (pp. 458, 459)

On the question of the fourth right, to bid on the property, Mr. Justice Brandeis continued:

"The new Act does not in terms provide for 'the right to protect its [the mortgagee's] interest in the property by bidding at such sale whenever held . . .' But the committee reports and the explanations given in Congress make it plain that the mortgagee was intended to have this right. We accept this view of the statute." (p. 459)

In 1940 this Court modified its views on the second Frazier-Lemke Act in *Wright* v. *Union Central Insurance Co.*, 311 U. S. 273. Our argument, however, is confined entirely to what *the Congress must have intended in 1935* when it enacted the amendments to Section 77; and the citations of the *Radford* and the *Vinton Branch* cases and the quotations from the opinions of those cases are aimed solely to demonstrate the following:

(1) On May 27, 1935, this Court held that a bankruptcy statute [Section 75 (s)] which deprived a mortgagee of the right to retain his lien until the indebtedness thereby secured is paid, and the right to realize upon the security of his lien by a judicial public sale, and the right to protect his interest in the property by bidding at such sale whenever held, was a violation of the Fifth Amendment and consequently invalidated the statute in question.

(2) On August 23, 1935, the Congress passed a new amendatory statute aimed to correct the legislative errors in the First Frazier-Lemke Act that were pointed out in the *Radford* case.

> "Emphasis upon the deliberate intention to meet the constitutional objections raised in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, dominated the consideration of the bill in all stages." (Mr. Justice Brandeis, Footnote No. 9, in *Wright* v. *Vinton Branch*, 300 U. S. 440, at page 464)

The new statute preserved the rights of the mortgagee to retain his lien until the indebtedness thereby secured was paid, to realize upon his security by judicial public sale, and to protect his interest in the property by bidding at such sale (*Wright* v. *Vinton Branch*, 300 U. S. 456, 457-459).

(3) The same Congress passed the 1935 amendments to Section 77 just three days earlier, on August 20, 1935.

It is therefore wholly unreasonable to conclude that, in passing the amendments to Section 77, the Congress consciously intended to pass legislation *permitting* the substantive rights of a mortgagee to be struck down by the Interstate Commerce Commission in a Section 77 proceeding, when that same Congress was in the final stages of enacting a statute (viz. the second Frazier-Lemke Act) containing special provisions aimed at *preserving* the substantive rights of mortgagees, and thus curing legislative errors in an earlier statute (viz. the first Frazier-Lemke Act).

The following excerpts from the Congressional Record demonstrate how the two Bills passed through Congress virtually elbow to elbow and how the *Radford* case affected the debate on the two bills:

From the House debate on the amendments to Section 77 (August 15, 1935):

> "Mr. BURDICK. Mr. Chairman, I do not want to make any remarks on this bill. I have asked for

this time for the purpose of asking a question. I am submitting it to the constitutional lawyers of the House, not with the idea of trying to prevent the passage of this act, because I am for it myself; but I would like to have explained what the difference is between the procedure in respect to railroad companies and the procedure that we attempted to adopt under the Bankruptcy Act in reference to trying to save what was left of the farm homes. The Supreme Court on the Frazier-Lemke Bankruptcy Act, said that the bankruptcy law was passed, in the first instance, for the benefit of the creditors and not for the benefit of the debtors. I notice in this act there are certain circumstances which may arise when the court can order a reorganization without the consent of the creditors. I would like to have some constitutional lawyer—and there are many of them here—explain why you are sure that this law is constitutional, when we just found out that the one referring to farm lands was not constitutional.

"Mr. SUMNERS of Texas. Since no constitutional lawyers arise to consider the question, it devolves on the chairman to answer the question, if he can. *There is not very much similarity between this bill and the Frazier-Lemke bill**, *we believe*. I do not want to discuss the Frazier-Lemke bill, but I direct the gentleman's attention to one outstanding difference. The Frazier-Lemke bill sought to withhold the property mortgaged from the mortgagee, and at the same time reduce the amount of money which the mortgagor had promised to pay. I do not want to discuss that, but I will say this to the gentleman—and I appreciate the spirit in which he asked the question. We are hopeful that the inclusion of the language requiring the plan to conform to the law of the land** will meet the constitutional objections insofar as the law is concerned; but, of course, a given plan might not meet the test of constitutionality. It might be held that the plan did not itself

* Mr. Sumners is obviously referring to the first Frazier-Lemke Act.

** We respectfully point out that Section 5 of the Interstate Commerce Act which is discussed in the brief submitted on behalf of the St. Joe Paper Co. was part of the law of the land.

conform to the law of the land. According to our view, however, that would not affect the constitutionality of the law." (79 Cong. Rec. 13301) (Emphasis ours)

From the Senate debate on the second Frazier-Lemke Act (August 19, 1935):

"MR. ASHURST. * * * *Within a few hours we will probably have before us a bill affecting railroads* * * *" (79 Cong. Rec. 13640) (Emphasis ours)

From the Senate debate on the amendments to Section 77 (August 20, 1935):

"Mr. KING. Is there any provision in the bill which might be characterized as confiscatory of property and as authorizing, through the courts or otherwise, proceedings which would deny due process of law to persons who have interests in railroads, either stocks or bonds?

"Mr. WHEELER. None whatever." (79 Cong. Rec. 13764)

It is significant that in the *Radford* case the party to whom statutory relief was to be afforded at the expense of the mortgagee was an individual farmer whose financial misfortunes had been visited upon him by reason of circumstances beyond his control and that, notwithstanding, this Court upheld the security rights (as opposed to remedies) of the mortgagee. In the case at bar an affirmative answer to the question presented would serve to relieve not even a deserving debtor-mortgagor (for the rights of the stockholders of the Florida East Coast Railway have long since vanished) but rather the claim of a third party, the Atlantic Coast Line, which invokes the protection of this drastic interpretation of Section 77 in order to obtain ownership and control of a smaller railroad.

As Judge Hutcheson once said, in his earlier 1950 opinion:

"The case we have here is that of one railroad company coveting, and pressing to possess, a com-

peting debtor railroad company, against the wishes of 98 percent of the equitable owners of the debtor and over their violent objections, that consummation of the plan will result in depriving them of their property without just compensation." (*Atlantic Coast Line R. Co.* v. *St. Joe Paper Co.*, 179 F. 2d 538, 542)

Conclusion

Stripping this case to the essentials, the issue boils down to the following: In 1945, just as a satisfactory internal reorganization of the Florida East Coast Railway was about to be consummated, a majority of the Interstate Commerce Commission, in order to protect its concept of the public interest, decided that the railway should be merged with the Atlantic Coast Line Railroad at a price acceptable to the Coast Line, but unacceptable to the Mortgagee Trustees and the bondholders. In subsequent years the Commission has stuck stubbornly to that decision, justifying its action by asserting that the merger terms it had arranged are of substantial value to the First and Refunding bondholders who concededly own the equity.

This act of benevolent despotism is here challenged.

We respectfully submit that the purpose of Section 77 was to expedite the reorganization of insolvent railroads; and, for that purpose, to give the expediting agencies—the Commission and the courts—sufficient power to force recalcitrant minorities among creditor groups into line so that a reorganization could be speedily effected; and, as part of this perfectly understandable purpose, even to force into line the recalcitrant majority of a particular class of securities involved in a complicated reorganization (in the Missouri Pacific reorganization there were, it is said, 72 separate classes [MOORE'S BANKRUPTCY MANUAL, 1939 ed., p. 378, note 76]).

Considering this purpose, it is quite apparent that Section 77 has been perverted in this particular reorganization

to accomplish something entirely different. As pointed out, here there is for all practical purposes only one class of secured creditors who are interested in the reorganization. This class has a mortgage on substantially all of the debtor's property, and both mortgagees and their *cestui* bondholders are virtually unanimous in their opposition to the reorganization plan certified by the Commission.

If there has been delay in the reorganization of the Florida East Coast Railway, the party solely responsible since 1945 has been the Interstate Commerce Commission, which was entrusted by Congress with the task of eliminating delays.

In the light of the foregoing arguments, petitioners respectfully ask that this Court answer the question presented in the negative.

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Dated: September 21, 1953.

APPENDIX

Statutes Involved

Section 77 (b) (1) through (5) of the Bankruptcy Law, as amended, reading in part as follows:

"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price, the distribution of all or any assets, or the proceeds

derived from the sale thereof, among those having an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of defaults, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the charter of the debtor, and/or the issuance of securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; and may include any other appropriate provisions not inconsistent with this section."

Section 77 (e) (1) of the Bankruptcy Law, as amended, reading as follows:

"(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders;"

Section 77 (f) of the Bankruptcy Law, as amended, reading in part as follows:

"(f) Upon confirmation by the judge, the provisions of the plan and of the order of confirmation shall, subject to the right of judicial review, be binding upon the debtor, all stockholders thereof, including those who have not, as well as those who have, accepted it, and all creditors secured or unsecured, whether or not adversely affected by the plan, and whether or not their claims shall have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have, accepted it. Upon confirmation of the plan, the debtor and any other corporation or corporations organized or to be organized for the purpose of carrying out the plan, shall have full power and authority to, and shall put into effect and carry out the plan and the orders of the judge relative thereto under and subject to the supervision and the control of the judge, the laws of any State or the decision or order of any State authority to the contrary notwithstanding. The property dealt with by the plan, when transferred and conveyed to the debtor or to the other corporation or corporations provided for by the plan, or when retained by the debtor pursuant to the plan, shall be free and clear of all claims of the debtor, its stockholders and creditors, and the debtor shall be discharged from its debts and liabilities, except such as may consistently with the provisions of the plan be reserved in the order confirming the plan or directing such transfer and conveyance or retention, and the judge may require the trustee or trustees appointed hereunder, the debtor, any mortgagee, the trustee of any obligation of the debtor, and all other proper and necessary parties, to make any such transfer or conveyance, and may require the debtor to join in any such transfer or conveyance made by the trustee or trustees. Upon the termination of the proceedings a final decree shall be entered discharging the trustee or trustees, and making such provisions as may be equitable, by way of injunction or otherwise, and closing the case. Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, sale, con-

solidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan and not inconsistent with the provisions and purposes of chapter 1 of Title 49 as on August 27, 1935, or thereafter amended."

Pertinent Provisions of First and Refunding Mortgage, Florida East Coast Railway Company to Bankers Trust Company and Bethune W. Jones, Trustees, dated September 1, 1934

The Mortgage contains, following the usual recitals, the following granting clauses (p. 9):

> "The Railway Company, party of the first part hereto, has executed and delivered these presents, and has granted, bargained, sold, aliened, remised, released, conveyed, confirmed, assigned, transferred and set over, and by these presents does grant, bargain, sell, alien, remise, release, convey, confirm, assign, transfer and set over, unto
>
> "The Trustees, parties of the second part, their successors and assigns forever:
>
> "Part One
>
> "All and singular the railroads, railroad property and appurtenances, franchises, rights and privileges of the Railway Company, now owned, and any and all such property hereafter acquired by it, including the properties more particularly described in this Part One, other than the property in this indenture expressly excepted and excluded, and subject to the provisions in this indenture set forth and contained:"

Then follow four pages enumerating and describing the various assets of the railroad pledged under the Mortgage (pp. 9 through 15).

Then follow two habendum clauses (p. 16):

> "To Have and To Hold, the premises, railroads, rights, franchises, estates, appurtenances, leaseholds,

stocks, bonds and other property, real or personal,—hereinafter termed, collectively, '*mortgaged premises*'—hereby conveyed or assigned, or intended to be conveyed or assigned, or which may be conveyed or assigned to it by indentures supplemental hereto, unto the Trustees, their successor or successors and assigns, forever;

"SUBJECT, HOWEVER, as to the properties embraced therein or affected thereby, to the aforesaid First Mortgage, dated June 1, 1909, and, as to the properties covered thereby, to any and all prior mortgages, pledges and excepted rights recited or expressed in any indenture supplemental hereto executed as in this indenture provided:"

And finally the grant in trust, which reads (pp. 16-17):

"BUT IN TRUST, NEVERTHELESS, for the equal and proportionate benefit and security of all the present and future holders of the bonds and coupons issued and to be issued by the Railway Company and authenticated by the Corporate Trustee under this indenture, and for the enforcement of the payment of said bonds and coupons when payable and the performance of and compliance with the covenants and conditions of this indenture, without preference, priority or distinction as to lien or otherwise of any one bond over any other bond by reason of priority in the issue or negotiation thereof, so that, except as in this indenture otherwise provided, each and every bond issued and to be issued and authenticated as aforesaid shall have the same right, lien and privilege under this indenture, and so that subject to the terms hereof the principal and interest of every such bond shall be equally and proportionately secured hereby, as if all such bonds at any time outstanding had been made, executed, delivered and negotiated simultaneously with the execution and delivery of this indenture; and it is hereby covenanted and declared that all such bonds, with the coupons for interest thereon, are to be issued, authenticated and delivered, and that the mortgaged premises are to be held by the Trustees, upon and subject to the following covenants, conditions, uses and trusts; and it is covenanted between the parties hereto as follows—the term 'Railway Company' in-

cluding and meaning for all purposes of this indenture, the party of the first part hereto and any successor corporation as provided in Article Eleven of this indenture, viz.:"

At page 76, subsection 3 deals with the powers of the Trustees upon default, as follows:

"Sec. 3. In case of the happening of any of the events of default enumerated in Section 2 of this Article Seven, then and in each and every such case of default, during the continuance of such default, either (a) the Trustees (or, if the Trustees deem it to be advisable, the Individual Trustee alone) personally or by agent or attorney, with or without entry, in their or his discretion may sell subject to the liens thereon which then shall be prior and superior to the lien of this indenture, to the highest and best bidders, all and singular the mortgaged premises—including stocks, bonds, franchises, interest, appurtenances, and other real and personel property of every kind—and all right, title and interest therein and right of redemption thereof, which shall be made at public auction at such place and at such time and upon such terms as the Trustees or the Individual Trustee, acting therein, may fix and briefly specify in the notice of sale to be given as herein provided, or as may be required by law; or (b) the Trustees, or either of them, may proceed to protect and to enforce the rights of the Trustees and of the holders of the bonds secured by this indenture, by a suit or suits in equity or at law, whether for the specific performance of any covenant or agreement contained herein, or in aid of the execution of any power herein granted, or for the foreclosure of this indenture, or for the enforcement of any other appropriate legal or equitable remedy, as the Trustees or either of them acting therein, being advised by counsel, may deem most effectual to protect and enforce any of their rights or duties hereunder."

At page 80, subsection 9 of Article Seven provides:

"Sec. 9. Upon the completion of any sale or sales under or by virtue of this indenture, the Trustees shall execute and shall deliver to the accepted

purchaser a good and sufficient deed or other instruments conveying, assigning and transferring the property and franchises sold. The Trustees and their successors are hereby appointed the attorneys irrevocable of the Railway Company, in its name and stead, to make all necessary conveyances and assignments of property, and all necessary transfers of shares of stock and bonds or other obligations sold, and for that purpose they may execute all necessary deeds and instruments of assignment and transfer and may substitute one or more persons with like power, the Railway Company hereby ratifying and confirming all that its said attorneys, or such substitute or substitutes, shall lawfully do by virtue hereof. Nevertheless, the Railway Company, if so requested by the Trustees, shall join in the execution and delivery of such conveyances, assignments and transfers.

"Any such sale made under or by virtue of this indenture, whether under the power of sale herein granted or pursuant to judicial proceedings, shall operate to divest all right, title, interest, claim and demand, either at law or in equity, of the Railway Company, in and to the premises sold, and shall be a perpetual bar, both at law and in equity, against the Railway Company, its successors and assigns, and against any and all persons claiming or to claim the premises sold or any part thereof, from, through or under the Railway Company or its successors or assigns.

"The personal property and chattels conveyed or intended to be conveyed by this indenture, other than stocks, bonds and other securities and claims, shall be held and taken to be fixtures and appurtenances of the mortgaged railroads."

At page 82, subsection 13 of Article Seven provides:

"Sec. 13. Upon any sale as aforesaid, any purchaser, for the purpose of making settlement or payment for the property purchased, shall be entitled to use and apply any bonds and any matured and unpaid interest obligations secured by this indenture, by presenting the bonds and coupons hereby secured so that there may be credited as paid thereon the

sums applicable to such payment pursuant to the provisions of Section 12 of this Article Seven; and such purchaser shall be credited on account of the purchase price of the property purchased, with the sums payable out of such net proceeds on the bonds and coupons so presented; and at any such sale any bondholder or any other person may bid for and purchase such property, and may make payment therefor as aforesaid, and upon compliance with the terms of sale, may hold, retain and dispose of such property without further accountability therefor."

Following the execution of the Mortgage, it was filed for record or recorded, as the case may be, in each of 15 counties in the State of Florida in which the debtor's pledged property was situated (Mortgage, pp. 123-127).